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C O N F I D E N T I A L SECTION 01 OF 03 YEREVAN 000631

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SUBJECT: ARMENIA'S ENERGY SITUATION: DEALING WITH DEVILS

REF: YEREVAN 492

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Classified By: Amb. John M. Evans for reasons 1.4 (b, d).

SUMMARY

¶1. (C) While official Armenia insists that the incomplete Iran-Armenia gas pipeline was not included in the recent Hrazdan 5 energy-for-infrastructure agreement with Russia (reftel), the specific details of the midnight deal remain unclear. In response to the Ambassador's inquiries during May 2 U.S.-Armenia Task Force (USATF) meetings, Deputy Minister of Energy Areg Galstyan and Minister of Finance Vardan Khachatryan gave a wide-ranging overview of Armenia's energy situation, noting that the GOAM would continue to depend on the Armenian Nuclear Power Plant, Armenia's largest producer of electricity, until a comparable alternative -- a new nuclear power plant -- was installed. Galstyan also called for the refurbishment of Armenian gas storage facilities. Khachatryan said that, despite public criticism of the GOAM's decision to trade components of Armenia's remaining energy infrastructure to Russia, the sale of the incomplete 5th Unit of the Hrazdan Thermal Power Plant amounted to an Armenian victory over the Russians, who had to outbid the Iranians for ownership. Though he avoided specifics about the future of the incomplete Iran-Armenia pipeline, Khachatryan said Armenia would sell the pipeline "to the devil" if the devil would pay for the construction. End Summary.

U.S.-ARMENIA TASK FORCE DISCUSSES ENERGY

¶2. (C) At the semi-annual U.S.-Armenia Task Force (USATF) meetings May 2 in Yerevan, Minister of Finance Vardan Khachatryan and Deputy Minister of Energy Areg Galstyan sped through the GOAM's talking points on upgrading Armenia's natural gas storage capacity, decommissioning the old and building a new nuclear power plant, and developing Armenia as a regional energy hub. Khachatryan responded to the Ambassador's points about the need for transparency and launched into a passionate, wide-ranging monologue about Armenia's energy security strategy. Khachatryan forcefully defended the GOAM's decision to continue to operate the ANPP, to sell the 5th Unit of the Hrazdan Thermal Power Plant, and to seek the best price for the Iran-Armenia pipeline.

GOAM CONFIRMS COMMITMENT TO DECOMMISSIONING

13. (C) Deputy Minister of Energy Areg Galstyan took the lead on discussions related to the Armenian Nuclear Power Plant (ANPP) and said Armenia's position had not changed. He confirmed that the GOAM would be ready to move ahead with decommissioning as soon as alternative sources of energy were available. Galstyan explained that, based on recommendations made by USAID-contractor PA Consulting and others at the December 2005 IAEA-sponsored conference on decommissioning in Vienna, the GOAM had prepared a report on decommissioning and how best to build replacement capacity. Galstyan also said that the GOAM planned to host another meeting of international experts to discuss this matter in Yerevan in the near future.

UPGRADING STORAGE CAPACITY

14. (C) Galstyan underscored the need for increased energy security and said that Armenia needed to have a diversified energy sector. He mentioned that refurbishment of Armenia's gas storage facilities would greatly enhance Armenia's energy independence and estimated that storage upgrades would cost approximately USD 30 million. There was no mention of cooperation with Georgia on this project.

NEW NUCLEAR PLANT TO HELP MEET REGIONAL ENERGY NEEDS?

15. (C) In terms of building replacement capacity for the
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ANPP, Galstyan identified two scenarios, a thermal scenario and a nuclear one. He said that the nuclear scenario had "many advantages both in ecological and economic terms." According to Galstyan, the GOAM hopes to replace the current 400 megawatt ANPP with a plant with a capacity of 1,000 megawatts, both to meet Armenia's growing energy needs and because the GOAM believed the new plant "will have an important role in regional development."

16. (C) Ambassador Evans responded to Galstyan's comments saying that the U.S. appreciated the GOAM commitment to decommissioning and that, while the U.S. would continue to assist with safety upgrades for the plant, "any credible plan for safety upgrades must be based on a transparent end point." Evans explained that before the U.S. "would even consider supporting a feasibility study for a new plant, we (the USG) need to fully understand the strategy."

DECOMMISSIONING FUND: A GOOD IDEA, BUT...

17. (C) U.S. Department of Treasury representative Jeff Baker raised the issue of a decommissioning fund to help cover the costs of closing the ANPP. He said the IMF has identified the need to pay for decommissioning as the biggest threat to Armenia's long-term fiscal sustainability and suggested that Armenia should consider an additional energy tariff to help cover the anticipated costs. Khachatryan said the idea of a decommissioning fund was a good one, but that Armenia would not be able to cover the full cost of decommissioning itself and would need support from the donor community both for decommissioning and to develop replacement capacity.

THE PRESS OVERSTATES U.S. POSITION

¶8. (C) EUR/ACE Coordinator Tom Adams, Ambassador Evans and Minister Khachatryan also discussed decommissioning at a press conference following the USATF meeting. At the event, Adams said that the U.S. would consider helping Armenia pay for the research needed to make a final decision about replacements for ANPP and underscored the need for additional information before a final decision is made. He also raised concerns about building a second nuclear plant in a seismic zone. Some press reports erroneously interpreted Adams' comments as evidence that the U.S. was opposed to the construction of a new nuclear power plant in Armenia under any circumstances.

DESPITE PUBLIC OUTCRY, SALE OF HRAZDAN AN ECONOMIC VICTORY

¶9. (C) In response to Ambassador Evans' inquiries, Minister of Finance Vardan Khachatryan told the visiting USATF delegation that, far from a disaster for the GOAM, the decision to sell the 5th Unit of the Hrazdan Thermal Power Plant (TPP) was a "great deal." Khachatryan said that the Russians had expressed interest in Hrazdan's 5th Unit on several occasions previously, but that when Armenia announced the tender "they went silent." Khachatryan called the incomplete 5th Unit "a bunch of rotting rubble and rusty metal." The Russian offer (reportedly USD 248.8 million) was "just a gift, something we could not dream of," he said. According to Khachatryan Iran had offered about USD 140 million but sought about USD 60 million in co-financing from Armenia. Better than the Iranian deal, the Russian offer, Khachatryan said, allowed Armenia to retain the USD 60 million and gain an operational, upgraded facility. In terms of the potential political implications of the sale, Khachatryan said, "It doesn't matter what color the cat is, so long as it catches mice." "And besides," he said, "you should be happy the deal with Iran didn't go ahead. You should welcome this deal."

IRAN-ARMENIA PIPELINE: "WE'LL SELL IT TO THE DEVIL ..."

¶10. (C) The Iran-Armenia pipeline was not included in the Hrazdan energy-for-infrastructure trade, Khachatryan told the Ambassador. (Note: Gazprom announced on April 6 that, along with the transfer of control of the 5th Unit of the Hrazdan

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TPP, Russian would also gain control of 40 kilometers of the Iran-Armenia pipeline. Gazprom pulled the initial version of the press release from its website, and later posted an amended version which omitted reference to the Iran-Armenia pipeline as part of the deal (reftel) End note.) Saying that any discussion about the sale of the incomplete Iran-Armenia pipeline was "theoretical, because the pipeline doesn't even exist," Khachatryan said Armenia would "sell the pipeline to the devil," if the devil would pay for construction. "Whoever pays the money, will earn the right to construct it," he continued. Khachatryan estimated construction of the second phase of the pipeline would cost approximately USD 160 million.

¶11. (U) EUR/ACE Coordinator Tom Adams did not clear this cable.
EVANS